

STATE OF IOWA
PROPERTY ASSESSMENT APPEAL BOARD

Hy-Vee Food Stores, Inc.,
Petitioner-Appellant,

v.

Buena Vista County Board of Review,
Respondent-Appellee.

ORDER

Docket No. 09-11-0102
Parcel No. 10-34-326-004

On November 23, 2010, the above-captioned appeal came on for hearing before the Iowa Property Assessment Appeal Board. The hearing was conducted under Iowa Code section 441.37A(2)(a-b) and Iowa Administrative Code rules 701-71.21(1) et al. Petitioner-Appellant, Hy-Vee Food Stores, Inc., was represented by Attorney Douglas R. Oelschlaeger of Shuttleworth & Ingersoll Law Firm, Cedar Rapids, Iowa, and submitted evidence in support of its petition. The Buena Vista County Board of Review designated Attorney William R. Stiles of Schneider, Stiles, Serangeli & Mountsier, Des Moines, Iowa, as its legal representative and submitted evidence in support of its decision. The Appeal Board now having reviewed the record, heard the testimony, and being fully advised, finds:

Findings of Fact

Hy-Vee Food Stores, Inc. (Hy-Vee), owner of property located at 1250 N. Lake Avenue, Storm Lake, Iowa, appeals from the Buena Vista County Board of Review decision reassessing its property. The real estate was classified commercial for the January 1, 2009, assessment and valued at \$2,150,520; representing \$357,070 in land value and \$1,793,450 in improvement value. Hy-Vee protested to the Board of Review on the ground that the property was assessed for more than authorized by law under Iowa Code section 441.37(1)(b). The Board of Review denied the protest.

Hy-Vee then appealed to this Board on the same ground. Hy-Vee's Notice of Appeal stated the fair market value was \$1,200,000, allocated \$200,000 to land value and \$1,000,000 to improvement value.

The subject property is a 37,039 square-foot, concrete-block grocery store built in 1993 and renovated in 2008. The building also has 2496 square feet of finished mezzanine and 960 square feet of unfinished mezzanine. The improvements are in very good condition and have 10% physical depreciation. It is located on a 5.06 acre site with 110,000 square feet of concrete paving.

Thomas H. Slack, Appraisal & Consulting Services Group, Overland Park, Kansas, completed a summary appraisal report on behalf of Hy-Vee reflecting an effective date of January 1, 2009. Slack valued the subject property at \$930,000.

Slack testified at hearing regarding his three approaches to value. Using the cost approach, he chose four land sales ranging from \$1.14 per square foot to \$5.25 per square foot. Slack made substantial adjustments for size of -40%, -55% and -65%, as well as condition and location adjustments. These adjustments resulted in \$1.80 per square foot indicated value, or \$400,000 in land value for the subject property. His replacement cost new less depreciation for improvements was \$2,370,237, which he further reduced by \$1,800,000 (52.6%) in external obsolescence for net operating income loss. Slack calculated a final depreciated improvement replacement cost plus land value of \$970,000. The obsolescence adjustment is extremely large and basically renders the cost approach to be an income-driven approach to value.

Slack developed an income approach to value but stated this valuation method was not the best indicator of market value for the subject property because he opined that finding a tenant for this size of property in Storm Lake would be problematic. Using the income approach, Slack determined the subject property to have an estimated value of \$720,000. To determine gross income, Slack consulted with brokers who noted several properties with lease rates ranging from \$2.50 to \$6 per square foot.

Slack applied a \$3.50 per square foot rental rate. He believed that allowances for tenant improvements are increasing and are effectively lowering the rent rates to around the rate he selected. He adjusted for vacancy loss, and estimated the expenses to arrive at a net operating income (NOI) of \$101,001. Slack capitalized the net operating income using a tax adjusted 10.44% capitalization rate for a value of \$967,291, rounded to \$970,000. Slack reduced this value by adjustments for tenant improvements of \$74,078 and rent loss during lease-up of \$173,546 amounting to over 25% in reduction. This is unusual because it appears Slack's comparable rents already include reductions for tenant improvements. Using these "effective rates" and then later reducing the value again for tenant improvements would essentially account for this factor twice. Additionally, typically when determining NOI, vacancy accounts for rent loss during lease-up. Slack's adjustments resulted in an indicated value of \$722,376 rounded to \$720,000.

Slack ultimately placed little weight on the income and cost approaches and primarily used the sales comparison approach for his value opinion.

Slack's sales comparison approach started with a list of eighteen sales of big-box retail properties in Iowa built no earlier than 1990, but most of his analysis focuses on ten sales. Slack characterized the first six of these ten sales as "primary" sales, and sales seven through ten he characterized "secondary." Slack testified at hearing that he did not remember separating the sales into these categories but the appraisal report contains multiple references to the "primary" and "secondary" sales.

Sale one, the former Wal-Mart in Storm Lake adjacent to the subject, had been vacant for four years prior to purchase in December 2006 for \$700,000. After adjustments, Slack noted a value of \$13.26 per square foot. At hearing, the Board of Review introduced rebuttal evidence of easements and use restrictions as part of the sale. Slack was not aware of these restrictions and stated this sale could be less reliable depending on the magnitude of the sale restrictions. The Board of Review's

Exhibit E, evidence showing the easements and covenants, was not admitted at hearing until a complete and certified copy of the document was submitted to this Board and counsel for Hy-Vee. The certified copy was received, was admitted, and has been considered as evidence. Subsequent to the hearing, Hy-Vee filed Exhibit 13 in response to Exhibit E. We admit Exhibit E and give it little weight, considering Slack was not aware of the restrictions when completing the appraisal or at hearing and also considering the Board of Review does not have the chance to cross-examine the witness.

Sale two, Melander's TV, is located across the street from the subject and sold in August 2006 for \$280,000. While comparable in location, the Melander's building was built in 1971 and is much older than the subject. It is also not of similar construction. The large adjustment necessary for age/condition make this sale less reliable.

Sale three was the Hy-Vee building in Burlington, Iowa. Slack testified he relied heavily on this sale. This property sold in January 2008 for \$700,000, and the buyer intended on using it as a furniture store. Hy-Vee had been using the property as storage since building a new building next door in 2003. This property is situated on a narrow site with limited visibility from the street. When the Board of Review's appraiser, Kevin Pollard, testified regarding this sale, he stated he did not use it in his analysis because it had deed restrictions. Pollard testified that he spoke with the buyer who confirmed the deed restrictions and commented that the use restrictions did affect what he was willing to pay for the property. Slack did not testify regarding any deed restrictions nor did his appraisal reference them. We place less reliance on this sale for this reason.

Sale four was the Hy-Vee store at 100 SW 8th Street, Altoona, Iowa. Hy-Vee built the property in 1980, remodeled in 1991, and had a ground lease that expired in 2005, with an option to extend the lease for five years. It bought out its lease and purchased the property in June 2006 for \$2,012,250. Slack reported the sales price included approximately \$350,000 for the value of an 8400 square foot shop attached to property that was built in 1985. He also made a 25% downward adjustment for the

property's location in a bigger town. Slack testified there was "a bit of a captive buyer" issue with this sale. However, his appraisal does not account for this fact, even though he made an adjustment for "captive buyer issue" to sale six. This is a sale between a lessor and lessee and there was no evidence the property was listed and exposed to the market before the sale. This factor could make the sale price unreliable under Iowa Code section 441.21(1)(b).

Sale five was the former Wal-Mart in Carroll, Iowa. It sold in June 2008 for \$1,195,728. This sale had 71,191 gross leasable square feet as opposed to the subject's 37,039. Despite the comparable's larger size, a 20% upward adjustment was made for this factor. Typically, a downward adjustment is made to the sale price of larger properties. Besides this unusual adjustment, this sale appears to be a reasonable comparable.

Sale six, referred to as the Cub Foods in Iowa City, sold in October 2008 for \$3,600,000. Wal-Mart owned the building next door and purchased this adjoining parcel to expand its operation. The purchase of adjoining land is an abnormal sale under Iowa Code section 441.21(1)(b) as the purchaser is often willing to pay a premium for adjoining land to expand its operation. Slack made a 5% adjustment for a captive purchaser but did not adjust this sale for being in a bigger market than the subject. Without more information on the captive purchaser situation and without a location adjustment, we consider this sale but find it less persuasive.

Slack considered sales seven through ten as secondary sales, giving them less weight than the six primary sales. Sale seven sold in August 2004, sale eight in June 2004, sale nine in May 2003, and sale ten in December 2004. These properties had been vacant for at least four years prior to the sales and only one was adjusted 10% for vacancy. Both sales seven and eight were sold in bankruptcy or foreclosure actions and do not appear to be adjusted. They would be considered abnormal under Iowa Code section 441.21(1)(b) if not adjusted to eliminate the effect of factors which distort market value.

Slack considered the sales comparison approach to be a reliable indication of market value. Excluding the dated sales (sales 7-10), the remaining sales ranged in price from \$10.53 to \$59.22 per square foot. After adjustments for time/market conditions, age/condition, location/lot size, and physical condition of these sales, the adjusted range of value is \$13.26 to \$39.60 per square foot. Slack used sales three, four, and five to narrow his range of values. Relying on sale three as the best representative for the subject property, he chose an adjusted value of \$25 per square foot. He multiplied \$25.00 per square foot by 37,039 square feet to conclude a value of \$925,975, rounded to \$930,000.

In Slack's final reconciliation and final value opinion he testified that he relied most heavily on the sales comparison approach and determined a final value of \$930,000.

Kathy Croker, Buena Vista County Assessor, testified at hearing that the subject property was located on a busy highway with good public exposure. She indicated her office valued the property improvements using the *Iowa Real Property Appraisal Manual* to determine the replacement cost new less depreciation and then made market adjustments to reach a final value.

Kevin M. Pollard of Roy R. Fisher, Inc., Davenport, Iowa, testified at hearing regarding a January 1, 2009, appraisal report he completed on behalf of the Board of Review. He valued the subject property at \$2,100,000, allocated \$465,000 to land value and \$1,635,000 to improvement value.

Pollard developed the cost approach and determined a value of \$2,150,000 (rounded). He did this by using a land value as determined by market land sales, plus the replacement cost of the improvements minus depreciation. Pollard stated the effective age is fifteen years old considering remodeling done in 2008. Pollard valued the land at \$465,000 based on five land sales in Storm Lake. Three of the sales occurred in 2008 and the remaining sales were older. The price per square foot of the sales ranged from \$2.26 to \$6.42. Pollard adjusted the sale prices -20% to +20% for location and

-30% to -20% for size. Adjusted land sale prices ranged from \$2.07 to \$3.53 per square foot. The improvements were valued at \$1,677,820 using *Marshall & Swift*, after deductions of 37.5% for depreciation and 25% for external obsolescence

In developing the income approach, Pollard was unable to locate comparable leased property in the Storm Lake area. He noted that gross store sales can be used to determine market rents, but Hy-Vee would not provide the gross store sales to use this method. Pollard considered rents from Hy-Vee in Cedar Falls (\$7/sq. ft.), Hy-Vee in Sioux City (\$10.78/sq. ft.), Shnuck's in Bettendorf (\$10.70/sq. ft.), and a former Econofoods store in Waterloo (\$7.01/sq. ft.). Pollard noted that Hy-Vee in Cedar Falls leased the shell for \$7 per square foot and completed extensive tenant improvements at Hy-Vee's own expense. He also noted the Sioux City and Bettendorf properties were in larger markets and would support higher lease rates. Pollard considered the age, size, and location of the subject property and estimated the market rent for the subject at \$6.00. He applied a 5% vacancy, noting that while the property is 100% occupied, a reasonable investor would account for the possibility of future vacancies. Applying the lease rate and subtracting expenses, including 2% management fees and \$.20 per square foot for reserves, Pollard determined a net income of \$199,492. Pollard applied a 10% capitalization rate and determined a value of \$1,994,920, rounded to \$2,000,000.

In the sales comparison or market approach to value, Pollard used five state-wide grocery store sales. He expanded his search due to what he stated was a lack of sales in the Storm Lake area. He testified the ideal comparable to the subject is a grocery store sold from a grocer to a grocer. His five sales ranged in size from 12,021 square feet to 67,492 square feet; with overall sales prices ranging from \$550,000 to \$8,200,000 or \$45.75 per square foot to \$121.50 per square foot. Pollard adjusted the sale prices -35% to +5% for location, -20% to +10% for age/condition, +5% to +10% for quality, -10% to +5% for building size, +5% to +15% for land building ration, and other adjustments of -25% to +15% for vacancy, existing leases, and conversion to alternative use. Pollard reported there was no

way to quantify adjustments for time of sale. But he also stated it was obvious that any appreciation in the market since 2005 has been offset by the current economic conditions. The adjusted square-foot prices range from \$54.68 to \$59.67. He then used the adjusted range and estimated the value at the lower end to arrive at \$2,100,000 (rounded).

Pollard's sale one is a former EconoFoods in Dubuque. It sold in May 2010 for \$3,400,000, and was purchased for an alternate use. A 30% location adjustment was made to account for the comparable being in a larger community. Pollard also made a 15% adjustment to account for the fact that the property was vacant when purchased and was converted by the buyer for an alternate use. He reported the buyer was spending a considerable amount to remodel the building for use as offices. May 2010 is after the January 1, 2009, assessment date, but there is nothing that prohibits PAAB from considering the sale. *See Bartlett & Co. Grain v. City of Sioux City Board of Review*, 253 N.W.2d 86, 91-92 (considering a sale in the sales comparison approach that occurred the year after the assessment). We consider this sale and weigh it accordingly.

Sale two is a grocery store located in downtown Orange City. It was built in 1969 but substantially remodeled in 1999. Pollard adjusted the sales price upward to account for inferior construction and quality. Pollard noted Orange City is smaller than Storm Lake but that the presence of Northwestern College in Orange City had a positive impact on the local economy. This property sold in July 2008 for \$550,000 on contract. Pollard verified that the buyer put 20% down and was charged an interest rate similar to what banks would issue at the time. He noted a balloon payment in five years. Pollard was not aware a contract sale is abnormal under Iowa law. He then testified he did not believe an adjustment was necessary to account for the sale being a contract sale because he felt the terms were essentially the same terms as conventional bank financing, with the exception of the balloon payment after five years. Without more details on the contract we give this sale little weight.

Sale three is a former Dick's Supermarket in Maquoketa purchased by Fareway Stores in June 2008. It is similar in size to the subject and was purchased for continued operations as a grocery store. Pollard testified that Fareway paid \$2,500,000 for the property and approximately \$750,000 was allocated by Fareway to equipment and personal property, leaving the net sale for the real property at \$1,750,000. Offsetting adjustments were made to arrive at a value of \$56.75 per square foot. Pollard reviewed the itemized bill of sale and opined that several real property items, such as landscaping and wiring, were improperly allocated to personal property. If properly allocated, Pollard stated the sale price would be higher. Pollard confirmed with Fareway that it did not pay anything for the business goodwill of Dick's Supermarket. Pollard believed Fareway is a sophisticated buyer and found this to be a very good comparable sale. We agree this is a good comparable sale.

Sale four is a Hy-Vee store in Windsor Heights, Iowa. It sold in June 2007 for \$8,200,000. Pollard noted this property is located in a suburb of Des Moines, warranting a 35% location deduction to make it comparable to the subject. Pollard noted that the sale was among investors, involved a 1031 exchange, and the assumption of the underlying mortgage. Also, a 25% "other" adjustment was made to account for the property being vacant when sold and then converted to another use. In total, a 55% downward adjustment was made to the property. Pollard stated this large adjustment made the sale less reliable but that he included this sale to "demonstrate what a Hy-Vee store would sell for." Like, Pollard, we find this sale less reliable.

Sale five is a former Econofoods store in Waterloo, Iowa, which sold in July 2005 for \$4,530,000. The store was closed in early 2005 and sold to an investor with six years remaining on the lease. Like sale four, a downward location adjustment was made to account for the subject being in a much smaller town. Also, a 20% downward adjustment was made to account for the fact that the property was being converted into multi-tenant use. A total of 25% in adjustments were made for this property, as opposed to the 55% adjustments to sale four.

Pollard relied more on sales one, two, and three. These sales indicate a range of \$56.75 to \$58.34 per square foot, which was applied to the subject to reach a value of \$2,100,000. We place little weight on sale two because it is an unadjusted contract sale but note that excluding it does not affect Pollard's range. We find the range applied by Pollard to estimate a value under the sales comparison approach to be reasonable and supportive of the market value as of January 1, 2009.

Both Slack and Pollard performed the three recognized approaches to value and both are qualified appraisers. Each determined a different value for the subject property, and we must determine which of the two appraisals to give more weight. Neither appraisal was flawless. For example, in the income approach to value, Pollard testified that he erred by not separately itemizing reserves for replacement. But he stated this would have a minor impact on his opinion of value. On the other hand, we feel the large, unusual adjustments Slack made to the capitalized income limit the credibility of this approach. There was a large difference in the lease rates each appraiser used to determine gross potential income. It appears from the evidence and testimony that Slack's lower lease rate (\$3.50) was an "effective rate," reduced to account for tenant improvement allowances that he again subtracted from the capitalized net income. Ultimately, Pollard's income approach is more reliable and supports a higher value.

On cross-examination, Pollard was questioned as to whether his 18-month exposure period violated Iowa Code section 441.21(1)(b). Counsel for Hy-Vee quoted the definition of "market value" and interpreted this provision as requiring a twelve-month exposure period. This interpretation appears to be incorrect. This language does not require appraisers to assume a 12-month exposure period. Section 441.21(1)(b) defines market value and requires property to be valued in the assessment year based on sales between willing buyers and sellers. Pollard did not violate Iowa law by assuming an 18-month exposure and marketing period. He repeatedly testified he value the property for January 1, 2009, which would meet the definition of market value under section 441.21(1)(b).

The law requires comparable sales be used as the primary method for valuing properties. Iowa Code § 441.21(1)(b). The parties' appraisers each presented approximately two reliable, comparable sales supporting two markedly different values. Slack's appraisal fails to convince this Board that his determination of value accurately reflects the market value for the subject property as of the assessment date. We find Pollard's appraisal is more reliable. We note, however, that even if we found Pollard's appraisal unreliable, we would still find that Slack's appraisal, including his sales approach, fails to convince us the subject property is over-assessed. We have concerns with Slack's overall methodology in the sales comparison approach. For instance, Slack makes an upward adjustment for comparables that have larger building area than the subject property. It is more typical appraisal practice to make downward adjustments for larger properties. While Slack testified that he had completed a sensitivity analysis, claiming the larger properties of this particular property type would have less appeal due to exceeding the typical buyer's needs, he did not provide any support for this opinion. Given the atypical nature of the adjustment we believe this should have been included.

Both appraisers made adjustments to their respective comparable sales evidence. Slack testified his adjustments were "generally market derived" by comparing and analyzing differences in the sale compared to the subject. Slack stated he used paired sales to make adjustments to his comparable sale 3, but his explanation of this adjustment was more akin to the "generally market derived" adjustments made to his other sales. Pollard stated two adjustments for the effect of leases were "admittedly subjective." Pollard's other adjustments were made in the same manner as Slack's. Appraisers determine the amount or degree of adjustment by applying their appraisal knowledge and experience to the data gathered for the assignment. We find Slack offered no more market support for his adjustments than Pollard.

Reviewing all the evidence, we find the preponderance of the evidence shows the property was assessed for more than authorized by law as of January 1, 2009. But the value claimed by Hy-Vee, \$930,000, is not supported by the record.

Conclusions of Law

The Appeal Board based its decision on the following law.

The Appeal Board has jurisdiction of this matter under Iowa Code sections 421.1A and 441.37A (2009). This Board is an agency and the provisions of the Administrative Procedure Act apply to it. Iowa Code § 17A.2(1). This appeal is a contested case. § 441.37A(1)(b). The Appeal Board determines anew all questions arising before the Board of Review related to the liability of the property to assessment or the assessed amount. § 441.37A(3)(a). The Appeal Board considers only those grounds presented to or considered by the Board of Review. § 441.37A(1)(b). But new or additional evidence may be introduced. *Id.* The Appeal Board considers the record as a whole and all of the evidence regardless of who introduced it. § 441.37A(3)(a); *see also Hy-vee, Inc. v. Employment Appeal Bd.*, 710 N.W.2d 1, 3 (Iowa 2005). There is no presumption that the assessed value is correct. § 441.37A(3)(a). PAAB's decision must be sufficiently detailed to show the path taken through conflicting evidence but does not need to discuss and explain each and every fact in the record. *Terwilliger v. Snap-On Tools Corp.*, 529 N.W.2d 267, 274 (Iowa 1995).

Although we review the record as a whole and there is no presumption the assessment is correct, the taxpayer carries the burden of proof in this appeal. Iowa Code § 441.21(3). In order to shift the burden to the Board of Review the taxpayer must introduce competent evidence from two disinterested witnesses that the property is over-assessed. In this case, Hy-Vee only called one witness. It did not shift the burden to the Board of Review, which would have been required to defend its value.

Property is to be valued at one hundred percent of its actual value. § 441.21(1)(a). Actual value is the property's fair and reasonable market value. *Id.* "Market value" essentially is defined as the value established in an arm's-length sale of the property. § 441.21(1)(b). Sales prices of the property or comparable properties in normal transactions are to be considered in arriving at market value. *Id.* If sales are not available or market value "cannot be readily established in that manner," "other factors" may be considered in arriving at market value. *Heritage Cablevision v. Board of Review of City of Mason City*, 457 N.W.2d 594, 597 (Iowa 1990); Iowa Code § 441.21(2). "To determine whether other properties are sufficiently comparable to be used as a basis for ascertaining market value under the comparable-sales approach, [the Supreme Court] has adopted the rule that the conditions with respect to the other land must be 'similar' to the property being assessed." *Soifer v. Floyd County Bd. of Review*, 759 N.W.2d 775, 783 (Iowa 2009). "Similar does not mean identical, but having a resemblance; and property may be similar . . . though each possess various points of difference." *Id.* Determining comparability of properties is left to the "sound discretion" of the trier of fact. *Id.* Consideration should be given to size, use, location, and character, as well as the nature and timing of the sale. *Id.* This Board is "free to give no weight to proffered evidence of comparable sales which it finds not to be reflective of market value." *Heritage Cablevision*, 457 N.W.2d at 598.

In an appeal that alleges the property is assessed for more than the value authorized by law under Iowa Code section 441.37(1)(b), there must be evidence that the assessment is excessive and the correct value of the property. *Boekeloo v. Bd. of Review of the City of Clinton*, 529 N.W.2d 275, 277 (Iowa 1995). Findings are "based upon the kind of evidence on which reasonably prudent persons are accustomed to rely for the conduct of their serious affairs." Iowa Code § 17A.12.

Viewing the record as a whole, we believe Pollard's appraisal supports a minor reduction in the assessment. Slack's appraisal does not show that the assessment is excessive, and we do not believe that \$930,000 is the fair market value for the property. We find Pollard's appraisal the most credible

evidence of the property's fair market value and it supports a reduction in the assessment. Therefore, we modify the Hy-Vee property assessment as determined by the Board of Review.

THE APPEAL BOARD ORDERS that the January 1, 2009, assessment of the Hy-Vee property located in Storm Lake, Iowa, as determined by the Buena Vista County Board of Review, is modified to \$2,100,000; representing \$357,070 in land value and \$1,742,930 in improvement value..

Dated this 24 day of February, 2011.

Jacqueline Rypma
Jacqueline Rypma, Presiding Officer

Richard Stradley
Richard Stradley, Board Member

Karen Oberman
Karen Oberman, Board Chair

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Certificate of Service	
The undersigned certifies that the foregoing instrument was served upon all parties to the above cause & to each of the attorney(s) of record herein at their respective addresses disclosed on the pleadings on <u>2-24</u> , 201 <u>1</u>	
By:	<input checked="" type="checkbox"/> U.S. Mail <input type="checkbox"/> FAX
	<input type="checkbox"/> Hand Delivered <input type="checkbox"/> Overnight Courier
	<input type="checkbox"/> Certified Mail <input type="checkbox"/> Other
Signature	<u>[Signature]</u>